

Q&A

JOB LOSS: Starting Your Own Business

Every new phase of life brings many challenges. The Internal Revenue Service recognizes that the loss of a job can create new tax situations for you. The following information is provided to clarify possible tax implications.

Can I be an Employee and a Business Owner in the same tax year?

Yes. Under the tax law, you can be both an Employee and a Business Owner at the same time if you choose. The primary issue is to report all income on your return.

Where can I get information about starting my own business?

Publication 334, Tax Guide for Small Business and Publication 3207, The Small Business Resource Guide CD ROM 2002 provides tax related information. These publications contain information on starting your own business, record keeping, and deductible expenses. In addition, Publication 3207 contains all of the business tax forms, instructions and publications needed by small business owners.

What options do I have for organizing my business?

Under the federal tax code, there are three options: Sole Proprietorship, Partnership or Corporation. A number of factors may influence your decision about which structure is best for you including cost of start-up, exposure to risk or liability, financing and the tax implications.

What record keeping requirements do I have as a Sole Proprietor?

Generally, you should keep detailed records of your income and expenses for your business to prepare not only required tax returns but also financial statements to help in maintaining and growing your business. The same general rules apply for Partnerships and Corporations with some additional detail.

How do I report my business income?

As a Sole Proprietor, you will need to file a Form 1040, Schedule C or C-EZ and Schedule SE. For more information, please see Publication 334, Tax Guide for Small Business.

What kinds of taxes do I pay as a Sole Proprietor?

Taxes due on net self-employment income (total business income minus expenses) include income tax and self-employment (Social Security) taxes. Additional information is available in Publication 533, Self-Employment Tax. You may be responsible for Employment Taxes if you have employees working in your business, see Publication 15, Circular E, Employer's Tax Guide for details.

How do I pay my taxes as a Sole Proprietor?

Generally, you would pay using the 1040ES Estimated Tax process on a quarterly basis. Federal income taxes including Self-Employment tax use a pay-as-you-go system. You generally must make estimated tax payments if you expect to owe taxes of \$1,000 or more when you file your return. For more information on Estimated Tax see Publication 505. Employment taxes are paid using Forms 941, Employer's Quarterly Federal Tax Return, and Form 940, Employer's Annual Federal Unemployment Tax Return. The filing requirements for each of these forms and instructions about how to pay taxes due are included in the Publication 15, Circular E, Employer's Tax Guide.

Can I claim the Earned Income Credit on my net self-employment?

Net income from a Sole Proprietorship is earned income. The Earned Income Credit is available to taxpayers that meet certain income guidelines. See Publication 596, Earned Income Credit.

Are classes or seminars available to get additional information?

Yes. The Small Business/Self-Employed Division of the Internal Revenue Service has a number of Small Business seminars through out the nation. You can also order Publication 3700, A Virtual Small Business Workshop CD ROM or you can view it over the web at www.irs.gov/smallbiz. Other products are available to order at the Small Business Web Site as well.

Copies of the referenced publications can be found at www.irs.gov or you may call 1-800-829-3676.

